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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 1182

ROBERT E. DINEEN, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF LAWYERS MORTGAGE COMPANY, PETITIONER

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The *per curiam* opinion of the Circuit Court of Appeals (R. 177–179) is reported at 153 F. 2d 425. The findings of fact and opinion of the District Court (R. 154–168) is reported at 60 F. Supp. 37.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered February 6, 1946. (R. 179–180.) The petition for a writ of certiorari was filed May 1, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether Lawyers Mortgage Company, a corporation organized under the laws of the State of New York, was an "insurance company" other than "life or mutual" within the meaning of Section 204 of the Revenue Act of 1928, and as such taxable under that section on its income for the taxable year 1931.

STATUTE INVOLVED

The material provisions of the statute involved are printed in the Appendix, *infra*, pp. 12–15.

STATEMENT

This is a suit against the United States by the Superintendent of Insurance of the State of New York, as Liquidator of Lawyers Mortgage Company, a New York corporation, for refund of $126,576.12, plus interest thereon, paid by that company as federal income tax for the taxable year 1931. The basis of the suit is that Lawyers Mortgage Company was an insurance company, other than life or mutual, during that year, within the meaning of Section 204 of the Revenue Act of 1928, and that its income for 1931 was therefore taxable under the latter section rather than under the provisions of the Act applicable to corporations generally. (R. 2–14.)[1]

[1] Lawyers Mortgage Company previously had brought a similar suit for refund of capital stock taxes paid under the Revenue Act of 1921, c. 136, 42 Stat. 227, for the fiscal years ended June 30, 1922, and 1923, and this Court held that the

Most of the material facts were stipulated in the District Court. (R. 121–130.) On the basis of the stipulated facts, plus certain oral and documentary evidence introduced by the parties (R. 26–78, 83–117, 131–153), the District Court made findings of fact and conclusions of law (R. 159–168), and entered judgment for the Government (R. 169–170) which was affirmed on appeal (R. 177–180).

The facts found by the District Court (R. 159–167) are not in dispute. At all times material to this action Lawyers Mortgage Company was a domestic corporation organized and existing under the insurance laws of New York with its office and principal place of business in New York City. (R. 159–160, 163.)[2] On or about March 14, 1932, it filed a corporation income tax return for the taxable year 1931 on which it reported a gross income of $3,865,414.66, deductions of $1,593,579.71, taxable net income of $2,271,834.95, and a total tax due of $272,620.19 which was paid in installments during the year 1932. (R. 163.)

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company was not an insurance company other than life or mutual within the meaning of that Act for the years there involved. See *Bowers* v. *Lawyers Mortgage Co.*, 285 U. S. 182.

[2] In *Bowers* v. *Lawyers Mortgage Co.*, *supra*, this Court pointed out that although organized under the New York insurance laws the company confined itself in the years there involved mostly to business which also could have been carried on under the banking laws of that state. The record shows there was no change in that respect during the taxable year here involved. (R. 66, 158.)

Since the date of its incorporation in 1893, and including the taxable year 1931, Lawyers Mortgage Company always has been and is subject to regulation and examination by, and subject to supervision of the Superintendent of Insurance of the State of New York, has always been and is subject to the insurance laws of the State of New York applicable to title and credit guaranty companies organized thereunder, and, until the entry of an order by the Supreme Court of New York for rehabilitation of the company pursuant to state law, it was required to file with the Superintendent of Insurance, on forms approved by him, the statements required by him for each year. (R. 164.) The order of rehabilitation was entered on or about August 2, 1933, and thereupon the then Superintendent of Insurance took possession of the property and business of the company, as Rehabilitator, and proceeded to rehabilitate its affairs and deal with its property in its name. (R. 161.) The present action is being maintained by a successor in office of the Superintendent of Insurance who took over the business and property of the company in 1933. (R. 162–163.)

On September 13, 1934, Lawyers Mortgage Company, by the then Superintendent of Insurance of New York, filed a claim for refund of $136,310.10 (of which $126,576.12 is here involved) of the federal income taxes paid by the company for the year 1931. (R. 131–142, 164.) The principal ground on which that claim was

based (R. 141–142), and the only ground now urged in this action, is that in the year 1931, the company was an "insurance company" other than "life or mutual" within the meaning of Section 204 of the Revenue Act of 1928, and that therefore extension and lending fees aggregating $1,054,801.02 which it had reported as income for 1931 should be eliminated in determining its tax liability for that year. In connection with this issue the District Court found that the business carried on by Lawyers Mortgage Company during the year 1931 was substantially as follows (R. 165–167):

> Upon receiving an application for a loan it caused an appraisal of the proposed real estate security to be made and procured a title insurance company to certify the property, make a report as to title and insure the same. The person borrowing money from the company, having executed and delivered a bond and mortgage to the company, received from it an amount specified therein, less charges for title insurance, survey, disbursements and recording taxes.
>
> There was also subtracted from the amount given to the borrower by the company, a lending fee, some portion of which appears to have represented an appraisal charge. The appraisals were carried on by employees of the company, who worked on a salary basis.
>
> The loan would be sold either in its entirety or in parts. When the loan was sold

as a whole, Lawyers Mortgage Company delivered to the purchaser a contract called a "policy of mortgage guarantee." When a part of the loan was sold, a participation certificate was given to the purchaser indicative of the amount which he had paid therefor and purporting to represent his interest in the whole mortgage.

The "policies" and the certificates by their terms required the holders thereof by accepting the same from the company, to assign to the company all the rights in which they might share as mortgagees or assignees of the mortgages. Each "policy" or certificate contained a so-called guarantee by which Lawyers Mortgage Company guaranteed the payment of the principal amount thereof, as and when collected, but in any event within eighteen months following written demand made after maturity of the "policy" or certificate. Almost invariably the maturity date of the "policy" or certificate coincided with the maturity date of the mortgage loan with which it was connected.

The company further guaranteed the payment of interest to the purchaser of the "policy" or certificate at regular periods and at an agreed rate. This rate was usually ½ of 1% less than that specified in the bond and mortgage, but in some instances at least, the rate paid to the person purchasing from Lawyers Mortgage Company was identical with the rate received by Lawyers Mortgage Company from the

original borrower. Where the differential of ½ of 1% existed between the interest rate paid by the borrower and the interest rate paid by Lawyers Mortgage Company to the purchasers of "policies" and certificates, the company retained the difference and called it "premium." The company also retained the interest accruing between the making of loans on mortgage security and the sale of the "policies" and certificates. It also charged extension fees to the borrowers for the renewal of loans at the maturity dates of the bonds and mortgages.

The company made no assignment or apportionment of assets or income to the different parts of its business, but used them indiscriminately in its different activities. No part or portion of the expense of its various activities (e. g.) appraisement, bookkeeping, sales of certificates, preparation of documents, etc., was charged against any specific source of income.

The company at all times throughout the year 1931 owned first mortgages which were available for its guaranty fund pursuant to the then effective Section 173 of the Insurance Law of the State of New York, (Chapter 290, Laws of 1929). No specific mortgages were ever earmarked or segregated as being applicable to the guaranty fund. The statute in question did not require any segregation. No portion of the so-called "premium" described above was ever allocated under insurance risk.

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On the basis of this finding and testimony of one of the taxpayer's witnesses (R. 72), the District Court concluded (R. 167) that the character of the business carried on by the company in 1931 did not differ from the character of the business carried on by it in 1922 and 1923 and denied the claim for refund on authority of this Court's decision in *Bowers* v. *Lawyers Mortgage Co.*, 285 U. S. 182. (R. 154–159.) Its decision was affirmed by the Circuit Court of Appeals. (R. 177–179.)

ARGUMENT

There is no sufficient basis for granting certiorari in this case. As this Court pointed out in *Bowers* v. *Lawyers Mortgage Co.*, 285 U. S. 182, a company claiming the benefit of the insurance provisions of the income tax laws has the burden of showing clearly that it is an insurance company within the meaning of the applicable provision of law. This the taxpayer has failed to do, just as it failed to do so for the years 1922 and 1923.

1. There is no reason to grant certiorari in this case, as contended by the petitioner (Pet. 6), to determine whether mortgage guaranty companies are taxable as insurance companies or as ordinary business corportions. Each case depends on its own facts and the question was sufficiently settled for present purposes by this Court's decision in *Bowers* v. *Lawyers Mortgage Co., supra,* where it was pointed out (p. 188) that "the character of the business actually done in the tax years de-

termines whether it was taxable as an insurance company."

2. There is no merit to the petitioner's contention (Pet. 6–7) that the decision below is in conflict with the decision of this Court in *Bowers* v. *Lawyers Mortgage Co., supra,* or that the court below erred in failing to apply this Court's decision in *United States* v. *Home Title Co.,* 285 U. S. 191. The substance of petitioner's argument (Br. 9–12) seems to be that classification as an "insurance company" depends upon the ratio of so-called insurance income to total income. *National Commercial Title & Mtg. Guar. Co.* v. *Duffy,* 132 F. 2d 86 (C. C. A. 3d). But analysis of those cases justifies the conclusion that the character of the business which produced the particular income taxed is the determining factor, and the court below so held. The "character" of the business of the two companies was essentially different. The business of the Home Title Insurance Company was primarily the insuring of titles and guarantying mortgages. The business of Lawyers Mortgage was—and still is—primarily a lending business. It did not insure titles, and its guarantying of mortgages, although a lucrative source of income for the year involved, was only incidental to its loan business. Moreover, it has not been shown that the critical item of "premiums" represented insurance.

For the year here involved the taxpayer reported so-called "premiums" of $2,051,721.67,

which petitioner considers as representing approximately 48% of the taxpayer's income for the year. (Br. 12.) But, as this Court observed with respect to the taxpayer's "premium" income for 1922 and 1923 (*Bowers* v. *Lawyers Mortgage Co.*, *supra*, p. 189):

> The so-called premiums amount to about one-third of total income, but they cover agency and other services which generally are not performed under contracts of insurance. There is no showing that these amounts do not include profits arising from such sales or that they are justly chargeable or were intended to apply only to the risks covered.

Here the petitioner did not and could not establish that the so-called premium income was entirely allocable to insurance risks. (R. 58.) Compare *Lincoln Mortgage & T. Guar. Co.* v. *Commissioner*, 79 F. 2d 585 (C. C. A. 3d), certiorari denied, 296 U. S. 654. Furthermore, it is to be noted that the taxpayer's business included selling parts of a mortgage loan, represented by participating certificates, as well as whole loans (R. 166), and it is doubtful if such transactions involved any insurance risk whatever. Compare *Lawyers Westchester Mortgage & Title Co.*, 247 App. Div. (N. Y.) 895, affirmed without opinion, 272 N. Y. 553; *Matter of People* (*Tit. & Mtge. Guar. Co.*), 264 N. Y. 69, 88; *Title G. & T. Co.* v. *Mortgage Comm.*, 273 N. Y. 415.

3. The decision below is in harmony with Section 29.3797–7 of Treasury Regulations 111, promulgated under the Internal Revenue Code, and it is only by inference that petitioner seeks to show it is authority for holding that Lawyers Mortgage Company should be taxed as an "insurance company" for the year involved.

CONCLUSION

The decision of the court below is correct, and there is no conflict. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MAY 1946.